

**Office of Chief Counsel
Internal Revenue Service
memorandum**

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to: Valerie Liu, Director
(SBSE Technical Services)

from: A M Gulas, Acting STR, Branch 7
(Procedure and Administration)

subject: When a State Tax Return Should Be Obtained Under the SRFMI Program

This Chief Counsel Advice responds to your request for assistance. This advice may not be used or cited as precedent.

ISSUE

Under the State Reverse Match File Initiative, when should the Service acquire an actual copy of a taxpayer's State Tax Return rather than relying on Federal Adjusted Gross Income (FAGI) and Federal Taxable Income (FTXI) figures to substantiate the Service's position on adjustments to a taxpayer's account?

CONCLUSION

When using the SRFMI program, the Service should obtain a copy of a taxpayer's State Tax Return when a case becomes docketed or when the State Return is needed to perform an audit of the taxpayer as determined on a case-by-case basis.

FACTS

Exam currently is engaged in a program known as the State Reverse Match File Initiative (SRMFI). This project allows the Service to use information obtained from the States to determine taxpayers' deficiencies. Advice from this office has been requested to determine whether the actual State Tax Return is needed to substantiate a Statutory Notice of Deficiency (SND), or whether having FAGI and FTXI figures obtained from the States may serve as the basis for the SND.

LAW AND ANALYSIS

For a SND to be valid it "must 1) advise a taxpayer that [the Service] has determined a deficiency for a particular year and 2) either specify the amount of the deficiency or

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provide sufficient information to support the deficiency." Portillo v. Commissioner, 932 F.2d 1128, 1132 (5th Cir. 1991). A SND is "not invalidated because it contain[s] no particulars or explanations concerning how the alleged deficiencies were determined." Barnes v. Commissioner, 408 F.2d 65, 68 (7th Cir. 1969).

A deficiency assessment issued by the Service generally carries a presumption of correctness. Portillo, 932 F.2d at 1133 citing United States v. Janis, 428 U.S. 433, 441 (1976). That presumption generally prohibits a court from looking behind the Commissioner's determination into evidence used even though the determination may be based on hearsay or other inadmissible evidence. Dellacroce v. Commissioner, 83 T.C. 269, 280 (1984). That presumption does not carryover to instances where the government makes a "naked assessment" lacking a foundation. United States v. Janis, 428 U.S. 433, 442 (1976) (stating "proof that an assessment is utterly without foundation is proof that it is arbitrary and erroneous").

Unless the Service's deficiency lacks foundation, the burden of proof rests with the taxpayer to produce credible evidence at trial as to a factual issue. See IRC § 7491(a)(1); H.R. Conf. Rep. 105-500, at 240-241 (defining credible evidence as the "quality of evidence which, after critical analysis, the court would find sufficient upon which to base a decision on the issue if no contrary evidence were submitted). It is only when the taxpayer produces such credible evidence and complies with the requirements enumerated in IRC § 7491(a)(2) that the burden of proof reverts back to the Service. See IRC § 7491(a)(2). Producing credible evidence to satisfy the requirements of IRC § 7491(a) is a factual determination that is made at the time of trial.

Here, the Service is issuing SNDs based on the FAGI or FTXI received through the SRFMI program. These amounts have been self reported by the taxpayer on a signed State Tax Return and are considered admissions by the taxpayer. See Waring v. Commissioner, 412 F.2d 800, 801 (3d Cir. 1969); Lare v. Commissioner, 62 T.C. 739, 750 (1974); Kaltreider v. Commissioner, 28 T.C. 121, 125-126 (1957). These SNDs have a foundation. The burden of proof is therefore on the taxpayer to produce credible evidence refuting the determination. As discussed above, such evidence can only be shown at trial. If the taxpayer is successful, the burden of proof reverts back to the Service. Therefore, it is our recommendation that, once a case becomes docketed, the Service requests the State Tax Return for the individual taxpayers so it may be used in the event the burden of proof reverts back to the Service during trial.

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Please call (202) 622-7950 if you have any further questions.